

Hayward Says Oil Company Has Become Too Cautious

By Terry Macalister
The Guardian
26 September 2007

Tony Hayward, the new chief executive of BP, is to instigate a thorough management shake-up in an attempt to refocus the group following a "dreadful" third quarter and a deeper reappraisal of the business after the exit of his predecessor.

Shares in the group fell 3% to 572.5p as the City absorbed a downbeat assessment of BP's most recent operational performance - which will almost certainly hit revenues - from the former exploration and production boss, who took over the top job from John Browne on May 1.

Mr Hayward outlined new plans to slash management layers from 11 to seven, redeploying some staff and removing others to kick-start an oil group that, he believes, has become over-cautious despite the fatal Texas City refinery fire and other major accidents in the US.

He told a staff meeting of American workers in Houston that the company's share price performance, compared with that of its peers, was now at its lowest ebb since 1992. And he said delays bringing on stream high-profile field start-ups in the Gulf of Mexico, such as Thunder Horse and Atlantis, plus refinery difficulties at Whiting and Texas City, meant third-quarter revenues - to be formally released on 23 October - would be heavily reduced.

A BP spokesman confirmed last night that Mr Hayward had used plain words to spell out the difficulties suffered in the past three months as BP figures are also being hit by lower gas prices, depressed refining margins and higher costs. "Tony is a straight talker and he did say the operational performance of the company had been dreadful. He also made clear that there is a restructuring in train, which he hopes to [publicly] announce next month and which is not finalised yet," he said.

Sources close to the group said a review of the business since Lord Browne's exit had unearthed considerable "fat" and bureaucracy, which Mr Hayward was determined to remove. The new boss has decided that the structure of BP has become far too complex and fragmented, causing duplication and a lack of clarity.

"Assurance is killing us," Mr Hayward told US staff, noting that too many people were engaged in decision-making leading to excessive cautiousness, something that critics of its safety performance in the US might question.

The speech in Houston builds on comments made at his first press conference for BP's half-yearly results in July that the operating performance was "not good enough" and he wanted change, including a 25% cut in staff at the St James's Square HQ in a move to restore confidence.

Reporting a 12% slump in underlying second-quarter profits to \$5.3bn (£2.5bn), Mr Hayward said he would be doing things differently from Lord Browne, who fell from grace after a string of safety problems in the US before lying in court to try to keep his personal life under wraps. He pledged: "We can be more efficient, leaner and fitter by ensuring we have a common and consistent way of doing things; by reducing our overheads, and doing a better job at managing our third-party spend."

Earlier this month Mr Hayward distanced himself from the past by overseeing the departure of Anji Hunter, a former staff member at No 10 Downing Street, who had helped earn the company the unwanted nickname, Blair Petroleum.

Last night a friend of Mr Hayward said the BP boss was doing the right thing and claimed Lord Browne had been a man of ideas and big strategies but who had failed to keep down costs at a time when he was shielded by very high oil prices.

BP To Strip Out Four Layers Of Management

By Dearbail Jordan and Robin Pagnamenta
The Times
25 September 2007

BP's new chief executive, Tony Hayward, will cut four levels of management to remove a "lack of clarity" at the oil giant which is expecting to report "dreadful" third-quarter results next month.

He said that, relative to its peers, BP's share price was performing at its worst for almost 15 years. The remarks surprised investors who drove the shares down by almost 3 per cent to 572.5p.

A BP spokesman refused to comment on whether the company will make redundancies but it is understood that Mr Hayward's remarks applied to both operational performance, but that revenues would be hard hit.

BP employs 96,000 total staff in 100 countries and last year reported like-for-like third-quarter earnings virtually flat at around \$4.7 billion.

Mr Hayward said BP planned to simplify the business by cutting the number of layers of management between workers and the chief executive from 11 to seven.

He said: "There is massive duplication and lack of clarity of who does what. We will reduce the number of organisation units."

Mr Hayward also said BP needed to change its internal culture and become less risk-averse.

"Assurance is killing us," he said.

Mr Hayward made the remarks in a "town hall" meeting with middle management in Houston, Texas before circulating his comments in a confidential memo to staff.

BP reached a low point in the early 1990s, when oil was \$18 a barrel and it held £8 billion worth of debt. It was hamstrung by a boardroom rift under former chairman and chief executive Robert Horton, and was forced to cut its dividend.

Analysts expect third-quarter revenues to be hard hit

Barclays Wealth said in a note to investors: "Hopefully, the third quarter may mark a low point in the group's fortunes as the fourth quarter is expected to be better as several upstream projects come on stream and capacity is restored at Texas City and Whiting."

The fourth-quarter is expected to bring an addition of 250,000 barrels per day of production from the start of Atlantis, as well as other projects in Angola, Trinidad and the Gulf of Mexico.

But in the US, three of BP's five refineries are either not fully operational or production has been suspended.

At BP's Texas City refinery, where an explosion in 2005 resulted in the death of 15 workers, the plant is not yet up to full capacity but it is expected to reach 400,000 barrels-a-day by year-end and progress to full capacity of 470,000 barrels-a-day by 2008.

Its Whiting refinery, also not operating at full capacity, will be restored during the first half of 2008. However BP has not given a timetable when its Toledo plant will begin production after being closed for maintenance.

At the group's interim results - the first since he was appointed chief executive - Mr Hayward blamed weak engineering skills for delays at the Thunder Horse and Atlantis oil production platforms in the Gulf of Mexico.

Mr Hayward, who recently took over from Lord Browne of Madingley, has been scrambling to restore confidence in the group's operational record following the deaths of 15 workers at its Texas City refinery and an oil spill in Alaska in 2006.

The company has also faced problems in Russia, where, in June, the Kremlin tightened its grip on the country's energy resources by forcing BP to sell Kovykta, one of the world's largest undeveloped gas fields, to Gazprom.

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Notes from Tony Hayward's Town Hall Meeting September 19, 2007

By Laurie Beppler – As I heard it.

FYI – The BP Board is meeting in Houston for the first time. They visited Texas City. Today they were off to Thunderhorse. Tomorrow is the Board Meeting.

Safety, People and Performance are and continue to be our agenda.

* Safety – Making good progress in implementing the 6 point plan. The US OMS is being rolled out, not as quickly as expected, but being done correctly. Good indicators – Incidents are down and HIPOs are up (good reporting).

* People – Right people, right skills, right place, doing the right things. Deeply skilled, deeply professional.

* Performance – Relative to competitors has declines 30% and it is attributed to the financial performance. Lowest since the crisis of 1992-93. The big gap is a consequence of:

- Refinery – We do not have as much as Shell
- Missing revenues – Whiting, TX City, Upstream not online
- Complexity

Getting Revenues back on line. Third Quarter will be dreadful, but into 4th Quarter we will pick up 250,000 barrels/day of production from the start up of Atlantis (GOM), Plutonio (Angola), Mango (Trinidad), and smaller GOM projects. TX City and Whiting should be up to full capacity by the end of the year.

Complexity – Need to simplify the company. What we will and will not do. We're out of power generations with the exception of on our own property. We're out of H2 for transportation. We evaluating some countries where our only business is lubricants.

Simplifying the organization – First announcement in mid-October. We will reduce the number of organization units. Presently about 10,000 org. interfaces. Will reduce the number of layers from the workers up to the CEO from 11 to about 7.

ROOT CAUSE OF THE GAP – Behaviors & Culture. Need to engineer a shift in BP.

1. More pragmatic “back to business” approach.
2. Deep function, technical excellence – reinforce & reward.
3. Take well judged risks. Assurance is killing us. Need to sort out issue of assurance. Must take well judged risk based on deep functional, technical excellence.
4. Sustainable performance is based on continuous improvement.
5. Finish what we start, as opposed to new initiatives.

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6. Recognize we have a lack of consistency. Need a small number of standards and enforce them across the board. No more opting out.
7. Accountability – Get out of the mindset that everyone has a say in the decision. Person that is accountable takes the decision and reduces the recycle of decision making.
8. Leadership style that really listens.

Q&A

1. Implementation – see if the actions deliver results. 4Q – Revenue momentum into 2008. Challenge to keep momentum. From Revenue momentum to efficiency momentum.
2. Key metrics for performance – Does not see 2 or 3 silver bullet KPIs. Too simplistic to focus on 2 or 3 things. Need balanced focus. Characterize biz performance for each piece of the biz.
3. Diversity & inclusion – Need a work environment where everyone can bring in their whole self, don't leave part of yourself at the door. Everyone has a voice. Still have a ways to go with gender diversity and others.
4. SPU Structure – Look at simplifying the SPU. There is massive duplication & lack of clarity of who does what. The SPU is the fundamental building block to be strategic, but it needs to be as simple, efficient as we can make it.
5. GAP with Shell – per the revenue discussion, the gap will be closed in mid-2008.
6. People Management – Be in positions long enough to see the consequences of decisions. Completing what you started.
7. Org charts – Yes. (The Chairman's Exec Committee has also asked for them.) Will be provided in mid-October.
8. What is said about BP
 - a. Great exploration
 - b. Getting better at project execution
 - c. Great commercial innovation
 - d. Biggest, best trading enterprise in our sector
 - e. Great portfolio manager
 - f. Not a great operating company (This goes back to lack of consistency)
9. Buying back BP Shares –
 - a. Pay taxes
 - b. Grow the dividend in line with growth in the company
 - c. \$19 – 19.5 B invested back into the future
 - d. Cash – return to shareholders
10. Back to Business – Reality of doing biz in US – Oil & Gas is difficult. Extraordinary NIMBY, Fiscal take is unbalanced (could see change with change in Administration), Extraordinary inflation in the supply chain. Rise of nationalism in other countries with the rise in oil prices.
11. Climate Change (Asked by our own Tom Mueller) – The climate is being changed by human activity. Tony addressed the G8 Summit shortly after he became CEO.

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- a. E&P – Produce more oil & gas more efficiently with less environmental effects
 - b. Downstream – Produce more efficient products.
 - c. Alternative Energy – Beginning transition to lower carbon energy
 - i. We're serious about energy efficiency
 - ii. We're serious about 2nd/3rd generation biofuel – beyond ethanol
 - iii. Power generation with carbon capture & sequestration. Need to get practical about what we can do and others can't.
12. Managing Risk & Assurance – Multiple layers of assurance may not ensure that the risk is reduced at all. Best way to manage risk is technical excellence, good people. Need limited number of standards. Clean up assurance – does not need to be layer on layer. Individuals have to take accountability. Need to include ops in the redesign. Will build from the bottom up.

**Tony Hayward Townhall
Houston, Texas
September 19, 2007-09-19**

Notes

Introduction

- Thanked Houston staff for all their hard work and dedication to BP during these challenging times
- Said the agenda for his talk was on Safety, People and Performance with most of the emphasis on performance

Safety

- Making good progress in implementing the 6-Point Plan which is going a long way toward significantly reducing risk
- OMS implementation has begun in the US and while it is not happening as quickly as we would like, we are committed to take the time necessary to do it properly and to finish the job
- Recent safety indicators have all been positive including an increase in the reporting of High Potential Incidents (which is a good sign because it means that people are recognizing where we have the potential for problems and speaking up).

People

- Its about having the right people with the right skills in the right place and doing the right things
- We need people in every position who are deeply skilled and highly professional in what they do.

Performance

- Our performance today is very poor relative to our competitors.
- It has little or nothing to do with the negative press BP has been getting lately especially in the U.S. and all to do with our poor financial performance.
- In 2005 we used to produce about the same amount of profit as Shell. Since then the profit gap between BP and Shell has grown to about \$8 Billion.
- \$2 Billion in portfolio – we have less refining capacity than Shell and refining margins have been high
- \$4 Billion in missing revenues from lost revenues, such as refineries running at 50% and delayed major project startups
- \$2 Billion in higher costs due to our organizational complexity
- Due to all of these things, expect the third quarter to be absolutely dreadful
- We should see major improvements in Q4 due to the startups of Atlantis, Greater Plutonio, Mango in Trinidad and some smaller GOM Startups like Nakika
- By the end of this year, all of our refineries should be closer to full capacity
- We should close the entire revenue gap by the middle of next year.

How we will simplify the complexity in BP

- We will simplify our Business footprint in BP (where and how we participate)
- We are looking at where and how we will participate in convenience retail east of the Rockies
- We are looking at where and how we will participate in global lubricant markets
- We have decided to get out of hydrogen for transport and the power generation business except on our own facilities

Organizational Simplification

- We need to simplify our organizational complexity... the number of units and organizational interfaces
- Today we have more than 10,000 organizational interfaces in BP (1 for every 10 people)
- We need to reduce the organizational layers in the company between me and the frontline staff from the 11 we have today to around 7.
- There will be an announcement from me in mid-October on organizational simplification.
- What we discuss thus far are only the symptoms of the problem. Let's discuss what I think some of the causes are.

Causes of Organizational Complexity

- The root cause of these problems are behaviors and cultures
- We need to take a more pragmatic "back to business" approach
- The BP of today is at times too theoretical and intellectual
- We need to get back to the business of doing business and that means being prepared to take well-judged risks founded on deep technical competence.
- Assurance in BP is killing BP today

Continuous Improvement

- Sustainable performance is about continuous performance improvement
- We need to finish what we start and not introduce a new initiative every week
- We need to recognize that one of our biggest issues is a lack of consistency
- When we are good in BP we are amazing but when we are bad we are bloody awful
- To ensure continuous improvement and consistency we also need to have a brief set of standards that everyone, everywhere does in the same way. There is no longer an option to disregard these

Accountability and Decision-Making

- We need to reinforce points around accountability
- When a decision is taken, we can't keep going back and constantly revisiting it.
- But at the same time we need to have a leadership style that really encourages listening

Questions and Answers

How Important Is Internal Communications?

- I think internal communications is important. It is the lifeblood of the organization and as a consequence it needs to be staffed by experts who have the deep functional capability to do it right.

When will we start to see financial improvement?

- We will begin to see improvements in Q4 of 2007 and into Q1 and Q2 of 2008
- We then need to keep up the efficiency and revenue momentum going throughout 2008
- We can't claim to be a leader in the sector unless we get our financial performance up. To be seen as a leader you need to be seen as successful and profitable in the business.
- I am not a big believer in measuring our performance improvements by looking at just a few KPIs across the business. This is too simplistic and can get you in trouble quickly by causing all sorts of things to go wrong as has happened in the past.
- We need to establish a continuous improvement track in each part of the business that takes into account the specific needs of each business.

How will D&I be affected in the new culture?

- D&I is personally important to me and I believe we have made a lot of progress on this in the past five years.
- I believe we need to have a work environment where everyone feels they can bring all of themselves to work every day and not think they have to be someone their not in order to succeed regardless of their ethnicity, religion, gender, personality, etc.
- I want people to be themselves. That is something I have learned in my own career. The importance of being yourself and not someone who you think someone else wants you to be.
- I think we still have a long way to go in the D&I journey especially in the area of gender diversity at all levels of the organization.

How do we balance Decision-Making with Listening?

- Everyone does not need to have a say in every decision. We have to hold individuals accountable for making decisions but we also need to trust and verify that decision-makers are consulting with other and listening and that these are factored into decision-making
- We will not always get it right but it is a lot better that everyone thinking they have the right to decide everything and that every decision taken gets revisited time and time again. We cannot recycle every decision.

What is likely to happen with the SPU Structure?

- The SPU is and will continue to be the cornerstone of the business because they each have the kind of scale needed to be very strategic.
- We are not only going to make changes to simplify complexity at the Group. What's good for the goose is good for the gander.
- SPUs need to look into the mirror and see what they need to do to reduce complexity
- This is not one size fits all. How each SPU looks at their organization will depend on the unique characteristics of individual SPUs. There is not one template that is the right answer.
- Each SPU needs to be as simple and efficient as we can make it.

How do we get away from people spending more time managing their career instead of managing the business?

- People need to stay in their roles long enough to see the consequences of the decisions they have taken
- There needs to be a cultural behavior shift that has more people accountable for finishing what they have started and not passing it on to the next person
- When we make our organizational announcement in October, we will also try and include an organigram so people will be able to visualize the changes we have made to simplify the organization and to remove complexity.
- We need to help people to be able to see how it works and where they fit.

How will these changes affect the Performance Contract?

- There should be a dramatic simplification of the Performance Contract
- It will still include a balanced scorecard and also a lot of individual judgment
- I don't believe in reconciliation and why you can't deliver what's on the contract
- We might have a scale that says if you deliver as expected, it's 100 points but if you have extraordinary performance it might be 200 points which all will factor into things like salary, bonuses, VPP, etc.

What would people say about the BP of today?

- We are fantastic at exploration
- We are getting better at delivering projects
- We are a great trading organization
- We are a great portfolio manager
- They would not say that we are a great operating company and that is a problem since more than 80% of our people work in operating the company
- That is why OMS is so important.
- Today our operating performance is very uneven. We are great in some places but not in others
- We need to become a great operating company and that is about consistent standards and a change in our operating culture
- These changes will not take us to a perfect end-state. What we have outlined is the direction we are going in. I am sure we will continue to fine tune and to make changes as we go.

What is our Investment Strategy Moving Forward?

- We invested \$19 billion in the company to grow the business
- We are looking to sustain a growth rate on average of 5% a year
- We don't have the organizational capability and the supply chain will not really handle a consistent or sustainable growth rate that is higher than that
- We are also looking to grow our dividend in line with the growth of the company
- We will continue to return the surplus cash to our shareholders because that is what makes the most sense in this market.
- We are investing in the business up to our capacity and the capacity of the supply chain.

What can we do to improve the business climate in the US?

- It is very difficult right now to do business in our industry both in the US and elsewhere
- I just had lunch with Rex Tillerson and he said it is the most difficult business climate in the industry that he has ever experienced in the company.
- People don't want to see investment in energy infrastructure in their backyard so it is difficult to clear these hurdles
- There is a lot of politics going on in the US with an unpopular President and even more unpopular congress and it is more than likely going to be this way until the next election.
- It is this political climate that has made situations like what happened with the Whiting refinery worse because of all the politics
- The rise of nationalism in places like Venezuela, Kazakhstan and the limits placed on us in Russia make this very difficult.

What about our commitment to climate change?

- We continue to believe very strongly that the climate is changing as a result of human activity and that we have to do something about it.
- I was invited to speak on the issue in Berlin at the G8 Summit
- What Beyond Petroleum means to me for the:
 - upstream business - finding ways to produce more oil and gas more efficiently and with less environmental impact
 - downstream business - produce more efficient products with less environmental impact
 - Alternative Energy Business - transitioning to a low carbon future that includes things like wind, solar, a new generation of biofuels, and carbon capture and storage for power generation
- We need to look at what we can do in this arena that others can't because of our size and scale
- The US is lagging behind in the climate change issue but we are seeing a lot being done in this area in Europe with a lot of new regulations on the horizon

What can we do to improve the assurance process?

- Right now we have multiple layers of assurance, too many layers
- I don't think that having all these layers of assurance reduce risk and it can actually increase it.
- The best way to reduce risk is to have deep technical competence where we need it.
- We need to have a limited number of standards but ones that everyone in the organization follows.
- We need to clean up the layers of assurance
- Individuals need to be accountable for risk and to manage it.
- It is also important than when we do establish rules and processes that we understand how they impact operations before we implement them
- That is what OMS is about and why we have created a framework for it but we are building it from the ground up.